

**2017**

# **Review of Piedmont Natural Gas Company's Gas Rate Stabilization Act Monitoring Report**



**SOUTH CAROLINA OFFICE OF REGULATORY STAFF**

**Review of Piedmont Natural Gas Company's  
Gas Rate Stabilization Act Monitoring Report  
for the period ending March 31, 2017**

Pursuant to S.C. Code Ann. Sections 58-5-430 and 58-5-440

**September 1, 2017**

South Carolina Office of Regulatory Staff

1401 Main Street  
Suite 900  
Columbia, SC 29201  
(803) 737-0800

## Introduction

On February 16, 2005, the Natural Gas Rate Stabilization Act ("RSA"), S.C. Code Ann. § 58-5-400, was signed into law. The South Carolina Office of Regulatory Staff ("ORS"), in accordance with the RSA, conducted an examination of Piedmont Natural Gas Company's ("Piedmont" or "the Company") Monitoring Report for the twelve-month period ended March 31, 2017 ("Review Period"). The examination was conducted for the purpose of determining the Company's compliance with the provisions of the RSA.

Pursuant to the RSA, the Company must file Monitoring Reports with the Public Service Commission of South Carolina ("Commission") and the ORS on or before June fifteenth. In Docket No. 2017-7-G, Piedmont filed its Monitoring Report with the Commission on June 15, 2017 ("Request"). The Company reported in its March 31, 2017 Monitoring Report an adjusted rate of return and return on common equity of 5.39% and 6.03%, respectively. The Company's calculation of additional revenue requirements totaled \$17,552,834, consisting of a \$17,223,522 margin increase accompanied by a \$329,312 increase for demand cost under-recovery.

In accordance with the RSA, ORS's audit reports are provided to the Commission, the Company, and made available to all interested parties no later than September first. ORS's review of Piedmont's Monitoring Report focuses on the Company's adherence to the RSA and applicable Commission Orders. This report details the results of ORS's examination.

## RSA Rates History

In accordance with the guidelines of the RSA, the Company is entitled to an adjustment in rates sufficient to achieve a return on common equity as set by previous Commission Order, currently 12.60%. Table 1 shows the requested and approved changes granted for several prior RSA filings and a comparison to the current filing.

**Table 1:**

Docket No.	Order No.	Amount Requested	ORS Proposed Revenue	Amount Granted	Approved Return on Equity	Rates Effective
2013-7-G	2013-750	\$4,494,748	\$4,307,857	\$1,912,387	11.30%	11/1/2013
2014-7-G	2014-822	(\$2,620,770)	(\$2,419,417)	(\$7,084,417)	10.20%	11/1/2014
2015-7-G	2015-732	\$8,994,755	\$8,688,604	\$3,898,604	10.20%	11/1/2015
2016-7-G	2016-705	\$14,910,332	\$12,727,664	\$7,655,078	10.20%	11/1/2016
2017-7-G	TBD	\$17,552,834	\$12,094,357	TBD	12.60%	11/1/2017

## ORS Review

ORS examines the operating experience reported by the Company for the Review Period together with the associated revenue requirement calculations. The results of ORS's examination of the Monitoring Report and the underlying financial records through March 31, 2017, are contained in **Schedule 1**.

**Schedule 1** presents the Company's operating experience, rate base and rates of return for the Review Period, and the accounting and pro forma adjustments which ORS has determined are necessary to normalize the Company's operations.

Utilizing the per book rate base of \$304,831,051, and income of \$17,979,950, a rate of return was calculated on per book operations of 5.90% with a corresponding return on common equity of 6.99%. ORS accounting and pro forma adjustments increased operating income to \$19,726,693, and decreased rate base to \$304,077,188. The return on common equity computed by ORS after accounting and pro forma adjustments was 8.10%. After the adjustments for the proposed margin increase of \$11,765,000 and the increase for demand cost under-recovery of \$329,357, operating income increased to \$26,980,674. The rate of return on rate base computed by ORS after the adjustments for the proposed margin increase and demand cost under-recovery is 8.87% with a corresponding return on common equity of 12.60%.

**Schedule 2** presents an explanation of the accounting and pro forma adjustments ORS recommends for the Company's Monitoring Report to conform to S.C. Code Ann. §§

58-5-430 and 58-5-440. For comparative purposes, the adjustments of both the Company and ORS are presented on Schedule 2.

## Capital Structure

S.C. Code Ann. § 58-5-440 contains requirements for the March Monitoring Report and states, “(1) if the utility’s earnings exceed the upper end of the range established in the order, the utility shall calculate the reduction in revenue required to lower its return on equity to the midpoint of the range established in the order; or (2) if the utility’s earnings are below the lower range established in the order, the utility shall calculate the additional revenue required to increase its return on equity to the midpoint of the range established in the order.” The range is 12.10% to 13.10% with a midpoint of 12.60% return on equity.

**Schedule 3** presents the calculation of the weighted cost of capital used by Piedmont in calculating its return on common equity both before and after its adjustments for the proposed increase. The rate base, as shown on Schedule 1, is allocated between long-term debt and common equity using the Company’s as adjusted capital structure. The amount of total income for return necessary, after pro forma adjustments, to cover an embedded cost rate of 4.67% on long-term debt is computed to be \$6,674,190. The remaining \$13,052,503 of income for return is associated with common equity, yielding a return on equity of 8.10%. The overall cost of capital after accounting and pro forma adjustments prior to the proposed increase is 6.49%. The cost of capital after the proposed increase is 8.87%.

## Rate Design and Allocation of Additional Revenue

S.C. Code Ann. § 58-5-440 states, “The proposed rate changes, filed by the utility, shall conform as nearly as is practicable with the revenue allocation principles contained in the most recent rate order.” ORS has reviewed and agrees that the Company’s proposed tariffs conform as nearly as practicable with the revenue allocation principles set out in the Company’s most recent rate order, which is Commission Order No. 2002-761 in Docket No. 2002-63-G. If the Commission approves the findings of ORS’s examination, the Company would then apply the change in revenue amount in proportion to the Company’s Request using the same criteria. ORS will verify the new rates generate the approved revenue change.

## Tariff Changes

ORS reviewed the Company’s proposed tariff changes. The changes include consolidating:

- Rate Schedule 221 (Residential Service – Standard Rate) and Rate Schedule 201 (Residential Service – Value Rate) into Rate Schedule 201 (Residential Service);
- Rate Schedule 202 (Small General Service – Standard Rate) and Rate Schedule 232 (Small General Service – Value Rate) into Rate Schedule 202 (Small General Service);
- Rate Schedule 252 (Medium General Service – Standard Rate) and Rate Schedule 262 (Medium General Service – Value Rate) into Rate Schedule 252 (Medium General Service).

The consolidation and closure of these rate schedules does not result in any changes to the charges for a given class of customers. Additional incidental changes were made to Rate Schedule 208 (Negotiated Service), Rate Schedule 243 (Experimental Motor Vehicle Fuel Service) and the South Carolina Service Regulations to reflect the rate schedule changes.

ORS does not oppose the changes as proposed by the Company.

## Revenue Verification

ORS verified the approved rates for April 1, 2016 through March 31, 2017 reflect actual revenues generated during the Review Period. ORS utilized the approved rates in effect at the time the Monitoring Report was filed to obtain the annualized revenues. ORS utilized the rate schedules effective November 1, 2016, and a pro-forma adjustment to revenue and expenses for the cost of gas as reflected in the Company's most recent Gas Cost Recovery Mechanism.

ORS verified the proposed revised tariffs in Schedule 2 of Piedmont's proposed rate adjustments will generate additional revenues of \$17,552,834. ORS's review determined the retail revenue target increase is \$12,094,357 instead of \$17,552,834 as proposed by the Company (See Schedule 7 of the Company's Request). ORS reduced the Company's Request by \$5,458,477 or 31.10%. The results of ORS's examination are shown on Schedule 1.

## Conclusions

ORS reviewed Piedmont's Monitoring Report and conducted an examination of the Company's books and records. ORS recommends the revenue change requested by Piedmont be reduced to \$12,094,357. The primary adjustment differences are related to the removal of merger related costs and the removal of 50% of incentive plans associated with earnings.

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Office of Regulatory Staff

1401 Main Street

Suite 900

Columbia, SC 29201

